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S E C R E T SECTION 01 OF 04 KABUL 000366

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TAGS: [ECIN](#) [ECON](#) [EFIN](#) [ETRD](#) [KCOR](#) [KCRM](#) [PGOV](#) [PINR](#) [PTER](#)
KTFN
SUBJECT: AFGHANISTAN: UNREGULATED HAWALAS (MONEY SERVICE PROVIDERS) PRESENT CRITICAL VULNERABILITY

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Classified By: DCM CHRISTOPHER W. DELL FOR REASONS 1.4 (b) and (d)

¶1. (S) SUMMARY. Hawalas or Sarafs represent the primary source of funds transfer within Afghanistan, accounting for an estimated 80-90% of total transfer among individuals and small businesses. While the majority of hawala fund transfers are for legitimate purposes, sensitive reporting continues to highlight this method as a primary tool used by insurgent operatives to move funds to and from the Afghan front. It is also a method frequently used by narcotic traffickers and corrupt officials to move illicit funds to other countries. Da Afghanistan Bank (DAB) the Afghan central bank estimates that there are more than 1,000 hawalas operating throughout Afghanistan; many of which have branches across South Asia, the Middle East, and in some major North American cities. Of the estimated hawalas operating in Afghanistan, DAB reports that 110 are licensed and of that, around 85 are submitting currency transaction reports (CTRs) on schedule. Importantly, all of the licensed and reporting hawalas are located in the Sherzada hawala market in Kabul. Despite some success on currency transaction reporting, the DAB is yet to receive any suspicious transaction reports (STRs) from licensed hawalas and has had difficulty providing supervision in Kabul and beyond. In the past year, the DAB moved to pay greater supervisory attention to money service providers (MSPs) of which hawalas are one type by adding a separate dedicated Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) unit. On February 4, the AML/CFT non-bank supervision unit (in coordination with the Attorney Generals Office and the Ministry of Interior) began enforcement action against several unlicensed hawaladars (those who operate hawalas) operating in Kabul. Despite recent progress, the AML/CFT unit remains ill-equipped and largely incapable of bringing Afghan hawalas into compliance in Kabul and the broader region a truth that allows insurgents and others to operate with little fear of detection or enforcement action. END SUMMARY.

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Current Picture: Tremendous Reliance on
Hawala in Afghanistan
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¶2. (SBU) Hawala or Saraf is primarily an informal method used for transferring monies between communities. Hawala

originated in the Middle East and South Asia, and evolved to service traditional trade routes that were not permissive to carrying large sums of money. The hawala process consists of three main functions: money exchange, the sending and receiving of money, and the settlement of those transfer transactions. More recently, hawaladars began offering traditional banking services such as holding money on account, making loans, and interacting (and maintaining business accounts) with the formal financial sector to settle transactions.

13. (SBU) According to Afghan officials and other reporting, the majority of Afghanistans financial flows pass through hawala and the remaining 10-20% pass through formal financial channels. The remaining transfers are typically done through physical movement (either through ground or air-based cash couriers). These informal financial flows are handled by an estimated 1,000 hawalas that widely range in size and operational connection throughout South Asia and the world (to include the United States and Canada). The major hawala markets in Afghanistan include: Kabul, Herat, Jalalabad, and Mazar-e-Sharif, Kandahar City, and Konduz. By comparison, total banking sector assets stand at \$1.68 billion (17% of GDP) and are spread across 15 banks (10 of which are Afghan owned). Reports vary, but most estimate that a mere 5-10% of the population of Afghanistan is banked with the formal sector. Therefore, it is not surprising that hawalas constitute such a large market share given that the formal financial system is relatively new to Afghanistan and inaccessible to many of the countrys inhabitants who reside in remote areas (or where their bank of choice does not yet have a branch). While this has started to change with the expansion of the formal banking sector and new offerings like cell phone company Roshans M-Paisa system (mobile

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payment by cell phone), hawala remains the transfer method of choice for the majority of the population. Importantly, hawala is seen by many in Afghanistan as a tested and trusted value-transfer mechanism that offers the following key benefits: i) reliability; ii) low cost; iii) convenience; iv) speed; and in most cases, v) anonymity.

Regulations: Existing Laws and Regulations

14. (U) In April 2006, the DAB issued a new regulation for licensing, regulating, and supervising money service providers (MSPs). The regulation applies to all individuals and legal entities providing money services in Afghanistan, whether or not the individuals and legal entities are domiciled in Afghanistan. The regulation outlines the following key areas: i) process by which a money service provider should file for a license; ii) how the DAB will decide on the license application; and iii) the manner in which the money service provider may operate, and how the DAB will supervise money service providers.

15. (U) The DAB money service provider regulation permits licensed operators to engage in: i) money transmission; ii) safekeeping of funds to the extent necessary in order to facilitate a specific transaction; and iii) check cashing. In addition, the regulation stipulates that the approved money service provider should be deserving of public trust, have a fixed operating address, agree to remain AML/CFT compliant and continue relevant training, and agree to abide by the terms of the Money Service Providers Licensing Agreement. Most Hawaladars are also licensed as Money Changers.

16. (U) The regulation also details the cost of an application (AF 15,000/ US \$300) and annual assessment fees: i) AF 10,000 for the first licensed location; ii) AF 5,000 for each additional license; and iii) AF 1,000 for each authorized agent, associate, and employee. In addition to the

application and assessment fees, the Ministry of Finance (MOF) imposes an annual standardized tax on licensed hawala operators regardless of annual transaction size and volume. This inequity has resulted in open disagreement between the Government of Afghanistan (GOA) and the hawaladars negatively impacting the DABs ability to successfully expand hawala licensing in Kabul and beyond.

Financial Supervision: A Lack of Capacity

17. (SBU) The Financial Supervision Department (FSD) at DAB remains weak in the area of AML/CFT. Within the FSD, the AML/CFT division is primarily responsible for administering AML/CFT legislation, conducting audits, licensing new institutions, overseeing money exchange and money service businesses, and acting as liaison between the financial sector in general. According to various sources (including officials within the DAB), the capacity of the FSD to expertly perform their AML/CFT responsibilities remains particularly weak. This weakness is especially acute in the area of money service provider supervision, which was recently formalized through the creation of the new AML/CFT division (including the addition of new staff). Currently, four individuals work in the AML/CFT division of the FSD. These individuals are young, untrained, and inexperienced for this task. Further compounding the problem, the AML/CFT division has not articulated a unified strategy to license new hawalas in Kabul or provinces beyond the capital. In a February 3 meeting with the Treasury AttachQ, DAB Governor Fitrat said he plans to add six individuals to the AML/CFT division and asked for further training and planning assistance in this area. He also vowed to take more aggressive action against unlicensed hawalas over the next several months.

Hawala Licensing and Supervision in Kabul

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18. (SBU) Unlike banks in Afghanistan, the majority of hawalas remain unlicensed and unsupervised by the DAB. Currently, there are 110 licensed hawalas in Afghanistan. These hawalas are all located in Kabul, and of those registered, approximately 85 submit currency transaction reports to the Financial Transactions and Report Analysis Center of Afghanistan (FINTRACA) which functions as the Afghan financial intelligence unit. Hawalas (and other MSPs like Roshans M-Paisa) are required to submit all transactions regardless of amount to FinTRACA on a monthly basis. If estimates are correct, less than 10% of the hawalas in Afghanistan are licensed and compliant with DAB regulations. Moreover, DAB has not fully executed its supervisory authorities even in Kabul, as there are an estimated 400 hawalas operating there.

19. (SBU) On February 4, the AML/CFT non-bank supervision unit (in coordination with the Attorney Generals Office and the Ministry of Interior) began enforcement action against several unlicensed hawaladars operating in Kabul. The licensing team padlocked several hawala shops and instructed the owners to report to the DAB to apply for an authorized license. In an effort to reopen their businesses, the hawaladars followed directions and promptly applied for a license to legally operate. Hawala licensing efforts in Kabul will continue through the end of February.

Hawala Licensing and Supervision Beyond Kabul

10. (SBU) To date, DAB has not licensed any hawalas beyond Kabul. On several occasions, the Treasury AttachQ office has

met with Governor Fitrat and First Deputy Governor Safi on the importance of: i) ensuring that all hawalas operating in Kabul are licensed; and ii) expanding the licensing regime beyond Kabul. Following a variety of meetings on the subject, DAB First Deputy Governor Safi gave instruction to FinTRACA and the AML/CFT division to coordinate and devise a strategic approach that will region-by-region bring hawala operators into compliance and put into place a workable supervisory regime. To date, directives from the First Deputy Governor have not been fully acted upon.

¶11. (S) Lack of licensing outside of Kabul is disappointing. While certain areas such as Helmand and Kandahar present real operational obstacles to hawala licensing, other areas are more permissive for hawala registration. For example, Governor Fitrat instructed the AML/CFT division to begin hawala licensing in Jalalabad in March following completion of their efforts in Kabul.

¶12. (S) Based on sensitive reporting, the Treasury AttachQ office estimates that there are roughly 80-100 medium-to-large hawalas in Jalalabad; 150-180 in Herat; and 50-70 in both Mazar-e-Sharif and Kandahar City.

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Lack of Hawala Licensing Presents Serious Vulnerabilities for Exploitation
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¶13. (U) Incomplete hawala licensing in Kabul and lack of hawala licensing in key provinces represents an important systemic vulnerability. In 2005, the Financial Action Task Force wrote: Experience over the last decade has shown that alternative remittance systems can be misused for illegal purposes, including for both money laundering and terrorist financing.

¶14. (S) This observation is especially prescient in Afghanistan for several reasons. First, unlicensed hawalas operate with complete anonymity within Afghanistan, transferring money for both legitimate and illegitimate purposes tied to the insurgency, terrorism, corruption, and narcotic trafficking. In Helmand and Kandahar alone, the United Nations estimates that 80-90% hawalas operating there are transferring money connected to narcotic trafficking at the rate of close to \$1 billion annually. Second, those

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hawalas that are licensed also largely operate with anonymity due to lax DAB supervision. This picture is further complicated by the fact that many hawalas have accounts with Afghan banks. In a January 2 meeting, an unlicensed hawaladar operating in Jalalabad told the Treasury AttachQ office that he maintains a business account with Kabul Bank to transfer money and settle payments with other hawaladars operating in Afghanistan and Pakistan. Like the hawalas, these banks are regulated by DAB supervision. Deficient AML/CFT supervision of the banks and hawalas presents an increasingly complicated and concerning situation.

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Toward Enhanced Regulation
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¶15. (S) Moving forward, greater analysis of the hawala structure in Afghanistan and the broader region is necessary. The GOA has renewed its commitment to hawala licensing in Kabul and throughout the country with near-term focus in permissive regions such as Nangahar, Herat, and Balkh (Mazar-e-Sharif) provinces. The logical first expansion point is Nangahar (Jalalabad) given its proximity to Kabul, the large assistance footprint the USG maintains, and the urging of DAB Governor Fitrat to address this province next. Moreover, the larger donor community aims to make Nangahar a model province moving forward. With that in mind, Nangahar may afford itself to incentive-based thinking when

it comes to hawala licensing and regulation.

¶16. (SBU) As part of their commitment to regulating hawalas, the GOA must develop an integrated strategy that includes the following elements: i) hawala licensing information campaign (particularly on the law and requirements in provinces other than Kabul); ii) regulatory and law enforcement action where appropriate; and iii) a seamless licensing and reporting process.

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COMMENT
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¶17. (S) The current situation is improving albeit slowly. Recent enforcement action and commitments from the DAB Governor are a positive step forward. However, despite recognized momentum, additional commitment, resources, and follow-through are necessary to ensure that the DAB is taking hawala licensing and supervision seriously. Hawala licensing and supervision represents an important component of broader efforts to mitigate systemic vulnerabilities and combat illicit financing in Afghanistan. Unlicensed hawalas represent a lost information collection point, as well as an open door for terrorists, insurgents, corrupt officials, and/or narco-traffickers to transfer funds at will with very little risk. Moreover, a workable solution for hawala licensing and supervision should be made a priority given the fact that it is so widely used for legitimate and illegitimate purposes. It is important to note that licensing and supervising money service providers (such as hawalas) is very new in Afghanistan. Complying with licensing procedures will represent a large cultural shift for hawaladars and will take time. To further assist in this area, Treasury and USAID are addressing this gap from both a policy perspective and through the provision of advisors.
END COMMENT.

WOOD